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SUBJECT: SOUTH AFRICA ECONOMIC NEWSLETTER APRIL 21 2006 ISSUE

¶1. Summary. Each week, Embassy Pretoria publishes an economic newsletter based on South African press reports. Comments and analysis do not necessarily reflect the opinion of the U.S. Government. Topics of this week's newsletter are:

- SA Telecommunication Costs High;
- Chinese Cars Will Be Available in SA;
- Bank Fee Report Due;
- Mboweni Worried About High Consumer Spending;
- Microlenders Report Released;
- OECD Report Views Improving Rural Infrastructure More Important than Land Reform;
- Environmental Taxes Proposed; and
- Housing Market Cools.

End Summary.

SA Telecommunication Costs High

¶2. Based on an annual survey conducted by NUS Consulting, South Africa's telecommunication costs are still quite high. Among 14 countries surveyed, South African costs for national long distance calls and cell phones are the highest. According to the survey, a three-minute national call (a call made over a distance of 320 kilometers) using a fixed-line phone costs $0.34 in South Africa while a similar call costs $0.08 in Sweden, the lowest call rate among the 14 countries surveyed. Similarly, a three minute national call on a cell phone costs $0.74 in South Africa while a similar call costs $0.16 in the U.S. South African fixed-line charges for local and international calls were the second-highest after those charged by operators in Belgium and the U.S., respectively. Even though Telkom had reduced its charges for national and international costs in 2005, the decreases do not match up to the widespread price reductions made by telecommunications operators in many other countries. According to NUS, Telkom's high telephone and internet prices could allow the second national operator to acquire some of Telkom's market share. In 2005, Telkom estimated that it could lose between 10% and 15% of its market share to the second national operator, expected to start in June. The United States, which has the lowest cell phone prices among the countries surveyed, is the most expensive country for international fixed-line prices. A three-minute international call from New York to London costs $0.78 while a similar call from London to New York costs $0.13. Also included in the survey were Spain, Germany, Canada, France, Denmark, Italy, The Netherlands, Australia

and Finland. Source: Business Day, April 18.

Chinese Cars Will Be Available in SA

¶3. Bidvest, a McCarthy Motor Holdings subsidiary, confirmed that it was trying to close a deal with motor vehicle suppliers in China to provide trucks, sports utility vehicles and minibuses from China starting the first quarter 2007. McCarthy would fund part of the cost of converting left-hand-drive facilities in China to right-hand-drive production. McCarthy will then have the rights to distribute the vehicles in South Africa and other right-hand-drive markets. McCarthy expects that the Chinese cars would compete with Tata, a low priced Indian car introduced in South Africa in 2004. Chinese-made vehicles would be subjected to costs such as a right-hand-drive premium, 32% import duty and high shipping costs of as much as R12000 a vehicle. China is expected to become a major vehicle exporter in the next few years and could pose a threat to the South African automotive industry, which contributes about 7.4% to GDP. Due to China's lower engineering and manufacturing input costs, it was able to make vehicles 40% more cheaply than both Japanese and Korean car makers. Source: Business Day, April 19.

Bank Fee Report Due

¶4. The Competition Commission will release a study of bank charges of South Africa's top four banks to see if consumers are paying too much for transaction and monthly fees. In June 2005, the Competition Commission asked for this study after a prior April 2004 study stated that the

top four banks stifled competition and led to high banking charges to the detriment of the poor and low income workers. The Commission can refer matters to the Competition Tribunal for prosecution. The Tribunal holds hearings and may fine companies 10% of revenue if they are found guilty of price collusion. The 2004 report asserted that South African banks charge fees on more transactions and have higher fees than banks in other countries. In addition, the 2004 report focused on the national payment system (the set of interbank transfer procedures circulating money) as a way of restricting bank competition. The upcoming report should focus on ways to ensure that smaller banks have equitable access to the payment system. South Africa's largest banks have higher returns on equity than most banks in Europe. Standard Bank, Africa's largest bank, had a return on equity of 25.2% in 2005, while ABSA, controlled by Barclays, had a return on equity of 27%. FirstRand, which controls the No. 2 banking group by assets in South Africa, had a return on equity of 30% in the six months through December 31 2005. These compare with an average of 16.2% among the 76 members of the Bloomberg Europe Banks and Financial Services Index. Source: Bloomberg, Business Report April 19; Business Report, April 20.

Mboweni Worried About High Consumer Spending

¶5. South African Reserve Bank (SARB) Governor Tito Mboweni warned of significant inflationary risks caused by strong credit extension and consumer demand along with rising international oil prices and a widening current account deficit. Strong consumer spending and economic growth tend to increase prices along with imports, putting pressure on the current account balance. Household debt levels have increased and savings declined, leading Mboweni to voice concern about the sustainability of consumer demand if interest rates rise. He viewed interest rate increases as more likely than reductions. However, he noted that the overall inflation picture

remains comfortably within the SARB targets, providing support for the views of some economists that interest rates will remain unchanged in 2006. Mboweni said the SARB's models forecast the targeted CPIX (consumer inflation less mortgage costs) rate peaking just below 5% in the first quarter of 2007, then subsiding to 4.6%, and remaining at that level until the end of 2008. Source: Business Times and IOL, April 19.

Microlenders Report Released

¶6. A study by the Micro Finance Regulatory Council (MFRC) on township based microlenders reports that there are 30,000 township microlenders serving 600,000 customers. However, there are only 300 microlenders registered with the MFRC. The survey shows that relationships with clients by these lenders are of a far more personal nature, with the majority of those surveyed having between 21 and 40 clients with an average loan size of between R500 and R1 000. These relationships tend to be long-standing, with new clients generally taken on via references and rather limited credit checks. The average loan - from registered and unregistered lenders - is around R750 ($125, using 6 rands per dollar). The period of the loans is also generally shorter than those of banks. The registered microlenders tend to have longer periods, while unregistered operators are more willing to lend higher amounts for between one and six months. The MFRC research shows that interest rates varied between 25% and 30% a month, which equates to between 300% and 360% a year. The MFRC study is the most recent and comprehensive into previously disadvantaged lenders to the township, informal settlement, and rural community markets. Source: Eastern Province Herald and Sunday Times April 18.

OECD Report Views Improving Rural Infrastructure More Important than Land Reform
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¶7. According to an Organization for Economic Cooperation and Development report on South African agricultural policies, land redistribution is not enough to alleviate South African poverty. The OECD asserted that given its

limited resources of water and arable land, South Africa should focus more on improving social services and infrastructure in impoverished rural areas. The report stated that lack of official skills and support for new farmers had hampered transformation in agriculture and resulted in a number of black farmers failing. It also pinpointed a lack of funding. The report is the first OECD report on the agricultural sector in South Africa. The South African government's target is 30% of farm land owned by blacks by 2014. So far, government has reached just under 4% of its target. Source: Reuters and Business Day, April 20.

Environmental Taxes Proposed

¶8. A discussion paper released by the National Treasury outlined options to reform South African taxes to include environmental charges aimed at reducing pollution. Historically, environmental taxes have been used to raise revenue without any concern for the environment. Examples include the Road Accident Fund levy, the customs and excise levy, the plastic shopping bags levy and the local government electricity surplus levy. In South Africa, environmental taxes account for 2% of GDP and approximately 10% of total tax revenue. Four options for reforming South Africa's environmental tax laws are considered in the discussion paper. The first option is to reform current environmental taxes. This would include reviewing the transport and solid waste sectors and may

include encouraging the use of cleaner transport fuels with leaded petrol being taxed at a higher rate than unleaded to discourage its use. The second option is to introduce entirely new environmentally related taxes such as an electricity consumption tax, a fossil fuel input tax, taxes on water use and on effluents. The third option is to provide incentives for environmentally friendly activities. These would include extending incentives to farmers for the eradication of noxious plants and the prevention of soil erosion as well as wider environmental and conservation-based land-use practices. The last option is to introduce tax incentives. Five broad tax incentives have been considered: the creation of environmental funds; partial marking of environmentally related taxes; the introduction of rehabilitation funds; accelerated depreciation allowances and a review of specific tax provisions. Source: Business Day, April 20.

Housing Market Cools

¶9. The latest quarterly First National Bank (FNB) residential barometer shows signs of a cooling, though buoyant housing market. In the major metropolitan areas, 60% of residential property sellers did not receive asking price in the first quarter of this year compared with just 29% during the first quarter in 2005, despite increasing confidence in the property market. Ed Grondel, the chief executive of FNB HomeLoans, said unrealistic price expectations by sellers and more buyer choice were the main reasons why sellers failed to obtain their asking price. Overall activity level in the housing market had increased 6.3% from 5.8% growth in the fourth quarter of ¶2005. Properties remained on the market for an average of eight weeks, compared with seven in the fourth quarter of ¶2005. FNB's residential property barometer is a forward-looking indicator of the residential property market based on quarterly perceptions of 150 real estate agents. Source: Business Report and Business Day, April 20.

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